Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
	)	CC Docket 96-45
Federal-State Joint Board on	)	
Universal Service	)	

COMMENTS OF SUREWEST COMMUNICATIONS

SureWest Communications, by its attorneys, hereby files these Comments in response to the *Public Notice,* FCC 04J-2, released August 16, 2004, seeking comments on high-cost universal support mechanisms for rural carriers. In these comments, SureWest supports the Joint Board's proposal to differentiate between small, mid-sized and large companies for the purposes of high-cost support. However, as discussed below, SureWest suggests different criteria for distinguishing those categories than those proposed in the *Public Notice*. Specifically, the Joint Board should recommend that the following categories of study areas be eligible for varying amounts of high-cost support:

-Study areas with <u>less than 50,000 lines</u>;

-Study areas with <u>less than 100,000 lines</u>; and

-Study areas with <u>less than 200,000 lines</u>.

SureWest asserts that the above categories reflect a more nuanced and accurate picture of the distinctions in economies of scale and scope of operation in study areas of different sizes. Additionally, SureWest advocates eliminating the use of statewide average costs in certain circumstances for the calculation of payments of High Cost Loop Funds (HCLF) for carriers that serve less than two percent of the nation's access lines ("Two-Percent Carriers").

I. Introduction

SureWest is a facilities-based provider of telecommunications services, located in Northern California. Founded in 1914 as Roseville Telephone Company, SureWest's subsidiaries provide incumbent local exchange, competitive local exchange, interexchange, cable television, broadband and PCS services. SureWest Telephone ("ST") is an incumbent local exchange carrier serving only one study area of 83 square miles in Placer County, California. ST currently serves approximately 134,000 access lines with only two wire centers. As a locally owned and operated company, ST takes pride in serving all of the subscribers in its community.

II. The Current Distinction Between "Rural" and "Non-Rural" Carriers is Flawed, Resulting in Improper Allocation of Federal High-Cost Funds.

In enacting universal service policies and regulations since the passage of the Telecommunications Act of 1996, the Commission has distinguished between two different sets of LECs for the purposes of provision of federal high-cost support funds. While the distinction between the two categories created by the Commission was based only on number of access lines served, rather than on the territory served, the two categories of LECs were nevertheless denoted by the Commission as "rural" and "non-rural" companies. In hindsight, the use of the terms "rural" and "non-rural" in the context of universal service reform was unfortunate. Such terms create the incorrect implication that the cost structure of a company is based solely on the location of the company's service area, rather than on factors such as economies of scale and scope, and other factors that result in high-cost service. Indeed, "non-rural" companies serve the majority of the rural subscribers in the country, while some "rural" study areas have lines in urban areas. Many companies serve dense population pockets in rural areas, and in those pockets, the cost of service can be less than that of certain "non-rural" areas. In this proceeding, the Joint Board has an important opportunity to more accurately target study areas where high-cost support is appropriate.

It was the Commission's unfortunate decision to use the terms "rural" and "non-rural" to categorize carriers for purposes of high-cost support that led it to adopt the statutory definition of "rural telephone company" to define the study areas receiving the high-cost support at issue here.[1] However, while the Commission recognized that there was no statutory requirement to use this definition, use of the statutory definition apparently was a convenient resolution of the question, once the Commission decided to distinguish between "rural" and "non-rural" carriers.[2] Unfortunately, the result of this decision based on convenience was the flawed allocation of federal high cost funds, and the improper denial of such funds to study areas that should receive it.

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[1] *Universal Service First Report and Order*, 12 FCC Rcd 8776 (1997) at para. 310, selecting the definition in 3(37) of the Communications Act, 47 U.S.C. § 153(37). While that statutory section provides multiple ways in which a carrier could be defined as a rural telephone company, most carriers that meet the definition appear to do so through fulfillment of subsection (D), by serving less than 100,000 access lines in a particular study area.

[2] *Universal Service Tenth Report and Order*, 14 FCC Rcd 20156 (1999) at para. 459; *aff'd on other grounds*, *Qwest Corp. v. FCC*, 258 F.3d 1191(10th Cir. 2001).

The flawed allocation of federal high-cost support is suggested in paragraph 8 of the *Public Notice*: some study areas served by holding companies with millions of access lines each are classified as “rural,” even though those companies have significant economies of scope and scale due to their size. However, other study areas are classified as “non-rural,” even though the costs of serving such areas can be higher, due to the fact that they are served by stand-alone companies that are much smaller, and thus do not have the same economies of scale and scope.

The impact of this flawed allocation of funds is that some study areas that otherwise deserve funding (those with high costs and service provided by a company lacking economies of scope and scale) do not receive it, while some study areas that are not high-cost do receive funds. Ultimately, it is subscribers who pay the price, or worse, cannot afford to pay the price, of this flawed allocation of funds.

Thus, SureWest believes that it is wise for the Joint Board to seek comments as to whether the definition of “rural” for purposes of high-cost support should be modified. The flawed distinction impacts subscribers not just in the study areas that currently receive inadequate or excessive funding recognized in the *Notice*, but may impact subscribers in other study areas in the foreseeable future. That is, in addition to the examples cited in footnote 26 of the *Notice* of study areas just over the 100,000 access line limit served by a stand-alone company, there are other study areas where the same set of facts could arise soon. For example, the Horry Telephone Cooperative pushes the limit while serving a single study area with approximately 98,000 access lines.[3]

In sum, the definition of "rural" for purposes of high-cost support should certainly be modified.

III. The Joint Board Should Create Multiple Categories of Study Areas Entitled to High-Cost Support.

In the universe of over 1,400 ILECs (not to mention competitive carriers), clearly there are more than two rational categories of carriers (i.e., "rural" and "non-rural") for the purposes of evaluating costs and high-cost support. As was noted above, the use of the terms "rural" and "non-rural", while evocative, is not always helpful. Although this distinction may work at the extremes (*e.g.,* carriers with 1,000 access lines or Bell Operating Companies), it is the cases in the middle where this approach breaks down.

Accordingly, SureWest supports the proposal (*Notice* at para. 14) to differentiate between small, mid-sized, and large companies for the purposes of high-cost support. However, the break points between these categories should be modified to better reflect the economies of scale and scope that drive a company's cost structure.[4] While an argument could be made for larger number of categories, at a minimum the Joint Board should recommend that the following categories of study areas be eligible for varying amounts of high-cost support:

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[3] *See, 2004 Phone Facts Plus Telephone Trends* (USTA), at page 31 (access lines as of December 31, 2002).

[4] In creating a different high-cost support mechanism for "rural" carriers, the Commission recognized that a major distinction between "rural" and "non-rural" carriers is economies of scale and scope. *Universal Service First Report and Order*, 12 FCC Rcd at 8936.

-Study areas with less than 50,000 lines;

-Study areas with less than 100,000 lines; and

-Study areas with less than 200,000 lines.

SureWest asserts that the above categories reflect a more nuanced and accurate picture of the distinctions in economies of scale and scope of different sized operations. While the *Notice* did not propose to include study areas with more than 100,000 access lines in the "rural" support mechanism, the fact is that operations in such study areas can in fact be high-cost, especially if that study area is the only one to which a carrier provides service. This is because the area being served may be high cost due to factors such as difficult terrain, and the fact that economies of scope and scale of such an operation are far less than those of larger carriers.[5] Indeed, the Commission's Part 36 rules recognize that carriers with more than 100,000 but less than 200,000 access lines can need support. *See* 47 C.F.R. § 36.631 (carriers with less than 200,000 access lines receive varying levels of support for loop costs greater than 115% of the national average cost). SureWest's proposal herein is thus consistent with the Commission's Part 36 rules.

SureWest recognizes that the Board may be concerned that adding the category of study areas with less than 200,000 lines may add to the size of the high-cost fund,

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[5] For example, such a study area would likely have only a few wire centers. As a result, the cost of purchasing a switch would be much higher for the company serving that study area than the cost to a BOC, which has thousands of wire centers, and thus gets bulk discounts on switches.

but it is very unlikely that any resulting impact will be significant. First, if necessary, the Board could add a condition that such study areas be the only study area of the serving carrier. This would substantially limit the number of such eligible study areas. Furthermore, other proposals in the *Notice*, such as taking into account holding company status, if adopted, will reduce the current size of the fund substantially more than any increase resulting from the proposal herein.

IV. The Board Should Eliminate the Impact of Statewide Averaging of Costs on HCLF Eligibility for Two-Percent Carriers.

A substantial problem in the current high-cost support system is the arbitrary exclusion of support for high-cost study areas as a result of basing eligibility on statewide average costs. SureWest believes that at the present time, only three states are eligible to receive HCLF for non-rural companies. Congress surely did not intend such an inequitable result when it enacted Section 254. This inequity should not be perpetuated in the policies for allocating support to smaller "rural" companies.[6] To alleviate this problem, SureWest proposes that study areas served by Two Percent Carriers in states below the national statewide average costs (and thus denied support) would be eligible to elect application of the rural high cost support formula on a wire center basis.

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[6] This inequity should also be eliminated in support mechanisms for larger "non-rural" companies.

V. <u>Conclusion</u>

The definition of “rural” for purposes of high-cost support must be modified, in order to remedy the flawed allocation of federal high cost funds, and the improper denial of such funds to study areas that should receive it. SureWest urges the Joint Board to recognize the needs of study areas served by mid-sized carriers, and adopt the three-tiered categories of study areas eligible for varying amounts of high-cost support set forth above. Additionally, SureWest urges the Joint Board to allow Two Percent Carriers to elect application of the rural high cost support formula on a wire center basis, in the circumstance described above.

Respectfully submitted,

SUREWEST COMMUNICATIONS

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October 15, 2004